Report

of the

Examination of

Ashland County Town Insurance Company

Butternut, WI

As of December 31, 2002

TABLE OF CONTENTS

Page

I. INTRODUCTION 1

II. REINSURANCE 6

III. FINANCIAL DATA 8

IV. SUMMARY OF EXAMINATION RESULTS 14

V. CONCLUSION 29

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS 30

VII. ACKNOWLEDGMENT 31

State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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November 21, 2003

Honorable Jorge Gomez
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2002, of the affairs and financial condition of

ASHLAND COUNTY TOWN INSURANCE COMPANY
BUTTERNUT, WI

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The last examination of this company was made in 1999 as of December 31, 1998. The current examination covered the intervening time period ending December 31, 2002, and included a review of such subsequent transactions deemed essential to complete this examination.

The Summary of Examination Results contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company was originally organized as a town mutual insurance company on August 17, 1901, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Farmers' Town Mutual Fire Insurance Company of Ashland and Price Counties. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there were no amendments to the articles of incorporation nor the bylaws.

A review of the certificate of authority revealed that the company is currently licensed to write business in the following counties:

Ashland, Bayfield, Douglas, Iron, Price, and Sawyer

The company is currently licensed to write property, including windstorm and hail, and non-property insurance.

A review was made of the policy and application forms currently used by the company. The company issues approved policies with or without endorsements for terms of three years with premiums payable on the advance premium basis. Policy fees charged policyholders are retained by the company.

Business of the company is acquired through 43 agents, three of whom are directors of the company. Agents are presently compensated for their services with a 15% commission for new business and a 10% commission for renewal business on all lines.

Agents have no authority to adjust losses. Members of the adjusting committee review losses. Adjusters receive $8.00 per hour with a minimum of 2 hours for each loss adjusted plus $.36 per mile for travel allowance.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The board of directors consists of nine members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term. The current board of directors consists of the following policyholders of the company:

Name	**Principal Occupation**	**Residence**	**Expiry**
Hans Brendalen	Retired	Glidden, WI	2004
Clifford Bruch	Retired	Butternut, WI	2005
John Burch	Delivery Driver	Butternut, WI	2006
Max W. Bruch *	Retired	Butternut, WI	2004

Ralph L. Poppe *	Restaurant owner - Insurance Agent	Benoit, WI	2004
Gerald Richardson	Farmer	Ashland, WI	2006
Randy Richardson	Farmer	Ashland, WI	2006
Linda M. Smart *	Secretary/Treasurer-Office Manager Ashland County Town Mutual Ins. Co.	Butternut, WI	2004
Florine Wartgow	Retired	Butternut, WI	2005

*Directors who are also agents are identified with an asterisk.

Members of the board currently receive $50.00 for each meeting less than four hours, $75.00 for each meeting over four hours, and $.36 per mile for travel expenses. Board members who participate in out-of-office training or seminars are reimbursed for reasonable meals and lodging.

Officers

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified.

Officers serving at the present time are as follows:

Name	Office	2002 Salary
Hans Brendalen	President	$2,137.00
Gerald Richardson	Vice President	265.00
Linda Smart	Secretary-Treasurer/Office Manager	25,583.78

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Adjusting Committee	Inspection Committee	Investment Committee
Ralph L. Poppe	Hans Brendalen	Max W. Bruch
Gerald Richardson	Ralph L. Poppe	Linda Smart
Hans Brendalen	Gerald Richardson	Florine Wartgow

Growth of Company

The growth of the company during the past five years as compiled from its filed annual statements was as follows:

Year	Net Premiums Earned	Net Losses and LAE Incurred	Policies In Force	Net Income	Admitted Assets	Policyholders' Surplus
2002	$173,472	$176,896	1,468	$(88,291)	$474,739	$199,021
2001	137,350	63,054	1,324	15,506	477,848	321,474
2000	150,073	125,010	1,282	(38,315)	463,106	306,791
1999	156,210	144,481	1,239	(41,804)	437,984	315,897
1998	157,273	128,499	1,266	(17,099)	500,292	362,228

The ratios of premiums written, gross and net, to surplus as regards policyholders during the past five years were as follows:

Year	Gross Premiums Written	Net Premiums Written	Ending Surplus	Writings Gross	Ratios Net
2002	$453,989	$216,949	$199,021	228%	109%
2001	387,658	149,935	321,474	121	47
2000	363,713	151,556	306,791	119	49
1999	346,272	143,466	315,897	110	45
1998	337,094	164,209	362,228	93	45

For the same period, the company's operating ratios were as follows:

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Earned Premiums	Loss Ratio	Expense Ratio	Composite Ratio
2002	$176,896	$100,007	$173,472	102%	46%	148%
2001	63,054	74,658	137,350	46	50	96
2000	125,010	67,410	150,073	83	44	128
1999	144,481	66,902	156,210	92	47	139
1998	128,499	69,127	157,273	82	42	124

The company has experienced a pattern of net underwriting losses, net operating losses and decreasing surplus over the four year period under examination. For the same time period, the company’s gross premiums and net premiums written increased 35% and 32%, respectively, and the number of policies in force increased 16%, while ending surplus decreased 45% to a December 31, 2002, balance of $199,021. For the calendar year 2002, the company’s underwriting expense ratio of 46%, was slightly higher than the Wisconsin town mutual average of 43%. Underwriting expense increased 34% due to the increased number of new policies and the increased amount of coverage. This drove up commission expense, payroll and supplies expense. Finally, the 2002 reinsurance contract change that discontinued the offsetting liability commission was factor in driving up the expense ratio. The Wisconsin town mutual average composite ratio for 2002 was 100% while the company's composite ratio was 148%.

As of December 31, 2002, the company's reported surplus of $199,021 was below the $200,000 minimum surplus requirement, pursuant to s. Ins 13.06 (3) (a), Wis. Adm. Code. The office may take further action on the company if the company continues to incur losses and reductions in surplus, resulting in a surplus amount that does not comply section Ins 13.06 (3) (a), Wis. Adm. Code.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

Reinsurer:	Wisconsin Reinsurance Corporation
Effective date:	January 1, 2003
Termination provisions:	By either party at any subsequent January 1, by giving the other party at least 90 days' advance notice in writing.

The coverage's provided under this treaty are summarized as follows:

1.	Type of contract:	Class A Non-property
	Lines reinsured:	Liability
	Company's retention:	None
	Coverage:	100% of each and every loss, including loss adjustment expense, subject to the maximum policy limits of: a. $1,000,000 per occurrence, single limit or combined for bodily injury and property damage liability b. $1,000,000 split limits, in any combination of bodily injury and property damage liability c. $5,000 for medical payments, per person; $25,000 per accident
	Reinsurance premium:	75% of net premium written
2	Type of contract:	Class B First Surplus
	Lines reinsured:	All property business
	Company's retention:	$50,000
	Coverage:	$50,000 or less in respect to a risk; on a pro rata basis up to 50% of such risk Over $50,000 in respect to a risk; on a pro rata basis up to $800,000 Pro rata portion of each and every loss, including loss adjustment expense, corresponding to the amount of the risk ceded
	Premium:	Pro rata portion of all premiums corresponding to the amount of each risk ceded

	Ceding commission:	A provisional commission of 15% ranging to an adjusted maximum of 35% as a result of development of the loss ratio between 65% and 45%
3.	Type of contract:	Class C-1 Excess of Loss
	Lines reinsured:	All property business
	Company retention:	$20,000 per occurrence plus $15,000 annual aggregate deductible
	Coverage:	100% of each and every loss in excess of $20,000 up to $30,000, including loss adjustment expense
	Reinsurance premium:	Sum of the preceding four years' losses incurred of the reinsurer, of the business year just completed, divided by the total of the net premiums written for the same period multiplied by 125% Minimum rate of 6% of current net written premiums Maximum rate of 23% of current net written premiums Rate for the current annual period is 23.0% Deposit premium of $43,800 payable in monthly installments with a minimum premium of $35,000
4.	Type of contract:	Class D/E Stop Loss
	Lines reinsured:	All property business
	Company retention:	Annual aggregate net losses up to 75% of the company's net premiums written, subject to a minimum retention of $125,000
	Coverage:	100% of annual aggregate losses in excess of the retention
	Premium:	Sum of the preceding eight years' losses incurred by the reinsurer, of the business year just completed, divided by the total of the net premiums written for the same period multiplied by 125% Minimum rate of 7% of the current net written premiums Maximum rate of 25% of the current net written premiums Rate for the current annual period is 7% Deposit premium of $14,400 payable in monthly installments with a minimum premium of $12,000

III. FINANCIAL DATA

The following financial statements were filed with the Commissioner of Insurance in the company's annual statement at December 31, 2002. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus".

ASHLAND COUNTY TOWN INSURANCE COMPANY
Statement of Assets and Liabilities
As of December 31, 2002

Assets	Ledger	Non-ledger	Not Admitted	Net Admitted
Cash in Company's Office	$ 75	$0	$0	$ 75
Cash Deposited in Checking Account	14,987	0	0	14,987
Cash Deposited at Interest	48,024	0	0	48,024
Bonds (at Amortized Cost)	114,526	0	0	114,526
Stocks or Mutual Fund Investments (at Market)	226,589	0	0	226,589
Premiums and Agents' Balances and Installments:				
In Course of Collection	3,943	0	0	3,943
Deferred and Not Yet Due	56,596	0	0	56,596
Investment Income Accrued	0	2,797	0	2,797
Reinsurance Recoverable on Paid Losses and LAE	2,457	0	0	2,457
Electronic Data Processing Equipment	1,783	0	0	1,783
Other Assets:				
Expense Related:				
Reinsurance Contingent Commission Receivable	2,962	0	0	2,962
Furniture and Fixtures	1,573	0	1,573	0
TOTALS	$473,515	$2,797	$1,573	$474,739

ASHLAND COUNTY TOWN INSURANCE COMPANY
Statement of Assets and Liabilities (cont.)
As of December 31, 2002

Liabilities and Surplus

Net Unpaid Losses	$ 62,865
Unpaid Loss Adjustment Expenses	663
Fire Department Dues Payable	528
Unearned Premiums	161,124
Reinsurance Payable	42,193
Amounts Withheld for the Account of Others	979
Payroll Taxes Payable (Employer's Portion)	298
Other Liabilities:	
Expense Related:	
Accounts Payable	127
Accrued Property Tax	66
Pension Payable	75
Non-expense Related:	
Premiums Received in Advance	6,800
TOTAL LIABILITIES	275,718
Policyholders' Surplus	199,021
TOTAL	$ 474,739

ASHLAND COUNTY TOWN INSURANCE COMPANY
Statement of Operations
For the Year 2002

Net Premiums and Assessments Earned		$173,472
Deduct:		
Net Losses Incurred	168,363	
Net Loss Adjustment Expenses Incurred	8,533	
Other Underwriting Expenses Incurred	100,007	
Total Losses and Expenses Incurred		276,903
Net Underwriting Gain (Loss)		(103,431)
Net Investment Income:		
Net Investment Income Earned		9,491
Other Income:		
Service Income		5,649
Net Income (Loss)		$ (88,291)

ASHLAND COUNTY TOWN INSURANCE COMPANY
Reconciliation and Analysis of Surplus as Regards Policyholders
For the five Year Period Ending December 31, 2002

The following schedule is a reconciliation of surplus as regards policyholders during the period under examination as reported by the company in its filed annual statements:

	2002	2001	2000	1999	1998
Surplus, beginning of year	$321,474	$306,792	$315,898	$362,228	$352,192
Net income	(88,291)	15,506	(38,315)	(41,804)	(17,099)
Net unrealized capital gains or (losses)	(34,855)	899	28,688	(6,071)	23,846
Change in non-admitted assets	693	(1,723)	521	1,545	3,289
Surplus, end of year	$199,021	$321,474	$306,792	$315,898	$362,228

Reconciliation of Policyholders' Surplus

A reconciliation of the policyholders' surplus as reported by the company in its filed annual statement and as determined by the examination is detailed in the following schedule:

Policyholders' Surplus per December 31, 2002, Annual Statement			$199,021
Item	**Increase**	**Decrease**	
Net Unpaid Losses	$ 4,941		
Adjustment to Advance Premium	1,099		
Total	$ 6,040	$	
Increase to Surplus per Examination			6,040
Policyholders' Surplus per Examination			$205,061

IV. SUMMARY OF PRIOR EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. EDP Environment — It is suggested that the company research for alternate approaches to upgrading its computer software or search for new software that will meet the company's business needs.

   Action—Compliance. Since the last examination the company has purchased new computers and accounting software and is satisfied with this arrangement.

2. Invested Assets — It is again recommended that the company comply with s. 610.23, Wis. Stat., and s. Ins 13.05, Wis. Adm. Code, regarding custody and control of its invested assets.

   Action—Compliance.

3. Invested Assets — It is recommended that the company obtain a safety deposit box to safeguard all investment instruments in a more safe and secure environment.

   Action—Compliance.

4. Transition into the New Investment Rule — It is recommended that the company's board of directors develop a written investment plan to come into compliance with the investment rule, and that the company discontinues purchases of investments not complying with s. Ins 6.20 (6) (c), Wis. Adm. Code, until an excess of Type 1 investments is attained.

   Action— Compliance.

5. Stocks and Mutual Funds — It is recommended that the company limit future investments in mutual funds to 10% of assets pursuant to s. Ins 6.20 (6) (b) 6, Wis. Adm. Code, unless otherwise permitted at "Type 2" investments under s. Ins 6.20 (6) (d), Wis. Adm. Code.

   Action—Noncompliance, see comments in the summary of current examination results.

6. Net Unpaid Losses — It is recommended that the company review its inactive claims on a periodic basis and update the status of these claims in the loss register, as required by s. Ins 13.05 (3) (f), Wis. Adm. Code.

   Action—Compliance.

7. Commissions Payable — It is recommended that the company report only commission due its agents on the annual statement designated line "commissions payable" in accordance with proper annual statement reporting.

   Action—Compliance.

8. Unearned Premium — It is recommended that the company discontinue double counting for deferred unearned premium in its unearned premium calculation, unless the net premium in-force is reported net of the deferred premium.

   Action—Compliance.

9. Reinsurance Payable — It is recommended that the company report all reinsurance balances on the designated annual statement line rather than net reinsurance payable balances with other unrelated accounts in accordance with proper annual statement reporting.

   Action—Compliance.

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the board of directors and any committees thereof, were reviewed for the period under examination and also for the subsequent period.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its three in house agents and it's out side agencies. The contracts include language indicating the agents will represent the company's interests "in good faith." The company works with several local agencies and requires the principal to sign this agreement.

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination with no apparent conflicts being noted

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Professional Liability	$500,000, $5,000 deductible
Fidelity bond	$100,000
Workers Compensation:	
Employee injury	Statutory
Employee liability:	$100,000
Each accident	$100,000
Each employee	$100,000
Policy limit	$500,000
Property Coverage	
General Liability	$500,000
Medical Expense	$5,000
Fire Legal Liability	$100,000
Commercial Contents	$25,000, $500 deductible
Crime	$5,000, $500 deductible

Underwriting

The company has a written underwriting guide. The guide covers all the lines of business that the company is presently writing.

The company has a formal inspection procedure for both new and renewal business. All new applications and renewal business are inspected by committee members independent of the risk under consideration and review.

Claims Adjusting

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The function of this committee is to adjust or supervise the adjustment of losses. Outside adjusters are used when a specific expertise is needed.

Policy Cancellations

After reviewing and testing policy cancellations, it was noted that the company is terminating policies for non-payment of premium 30 days after the actual effective date of the policy allowing the insured an additional 30 days of coverage for free. The company sends out the first premium notice 30 days in advance, stating that the premium is due and failure to pay will result in cancellation. The 2nd notice could be altered to state that the policy has expired (currently states “will expire”) and could be reinstated without a lapse in coverage if payment is received by a specified date. This would insure that the company would not be liable for losses during the additional time (grace period) they allow for the late payments. It is suggested that the company alter its 2nd and final notice of cancellation in order to limit the company's risk of claims after the policy has been canceled due to non-payment.

Accounts and Records

The examiners' review of the company's records indicated that the company is not in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained
2. A proper cash receipts journal is maintained
3. A proper cash disbursements journal is maintained
4. A proper loss/claim register is maintained
5. A proper general journal is maintained
6. A proper general ledger is maintained

Section Ins 13.05 (4) (b), Wis. Adm. Code requires that all disbursements over a specified amount be approved by more than one officer, director or employee of the company. The company has not been consistently following its board-established policy requiring two signatures on all checks over $1,000. During this examination, several checks were found to not contain the required second signature. It is recommended that the company adhere to its policy regarding check signatures in compliance with s. 13.05 (4) (b), Wis. Adm. Code.

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, test checked for proper signatures and endorsements, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2002.

The company is audited annually by an outside public accounting firm.

EDP Environment

Company personnel were interviewed with respect to the company's Electronic Data Processing environment. Access to the computers is restricted by passwords. Company personnel back up the computers weekly and these diskettes are kept off-site. The company has manuals documenting the use of its software which describes how to use the company's software, outlines the steps to complete specific tasks, and assists in the continuity of operations for seldom-used applications, training, or when staff turnover occurs.

Disaster Recovery Plan

The company has developed a disaster recovery plan which identifies the steps to be performed in case the company loses a key employee, is not able to access its computer, information on its computer is lost, or the office building is destroyed, to name a few contingencies. The company's disaster recovery plan appears to be adequate.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

(1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and

(2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

> Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employee's of the company.

The company is in compliance with these requirements.

Investment Rule Compliance

The investment rule for town mutuals allows them to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as "Type 2") provided that the town mutual has a sufficient amount of lower risk investments (referred to as "Type 1"). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

1.	Liabilities plus $300,000	$575,718
2.	Liabilities plus 33% of gross premiums written	425,534
3.	Liabilities plus 50% of net premiums written	408,755
4.	Amount required (greater of 1, 2, or 3)	575,718
5.	Amount of Type 1 investments as of 12/31/2002	248,335
6.	Excess or (deficiency)	(326,383)

The company does not have sufficient Type 1 investments. During the period under review, the company has not made any additional Type 2 investments.

The company has developed a written investment plan which was adopted on February 26, 2000. This investment plan is not consistent with s. Ins 6.20 (6) (c), Wis. Adm. Code, in that it does not consider the minimum amount of Type 1 assets (Item 4 above). It is recommended that the company's board of directors adjust its written investment plan to comply with the investment rule in accordance with s. Ins 6.20 (6) (c), Wis. Adm. Code, and that the company refrain from any purchases of investments not in compliance until an excess of Type 1 investments is attained.

ASSETS

Cash and Invested Cash **$63,086**

The above asset is comprised of the following types of cash items:

Cash in company's office	$ 75
Cash deposited in banks-checking accounts	14,987
Cash deposited in banks at interest	48,024
Total	$63,086

Cash in the company's office at year-end represents the company's petty cash fund. A physical count was made by the examiners during the course of the examination and the balance reconciled to year-end.

Cash deposited in banks subject to the company's check and withdrawal consists of one account maintained in a local bank. Verification of the checking account balance was made by obtaining confirmation directly from the depositor and reconciling the amounts shown thereon to company records.

Cash deposited in banks at interest represents the aggregate of four deposits in two depositories. Deposits were verified by direct correspondence with the respective depositories and by an actual count and inspection of certificates and/or passbooks. Interest received during 2002 totaled $1,498 and was verified to company cash records. Rates of interest earned on cash deposits ranged from 0.5% to 4.05%. Accrued interest on cash deposits totaled $22 at year-end.

Book Value of Bonds **$114,526**

The above asset consists of the aggregate book value of bonds held by the company as of December 31, 2002. Bonds owned by the company are located in the company's safety deposit box.

Bonds were physically inspected by the examiners. Bond purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in bonds was not in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Interest received during 2002 on bonds amounted to $8,064 and was traced to cash receipts records. Accrued interest of $2,333 as of December 31, 2002, was checked and allowed as a non-ledger asset.

The company has several investments in bonds, with a statement value of $33,115, whose rating dropped below a “bbb” and was not in compliance with the new investment rule; section Ins 6.20, Wis. Adm. Code. The investment rule prescribes that a town mutual shall divest itself of any investment that does not comply with the rule within three years of its noncompliance, unless the commissioner permits a longer period or requires a shorter period. Two of these investments are corporate bonds which mature before the permitted time period expires. The company plans to monitor the remaining investments and bring them into compliance within the time limit required of non-compliant investments.

Stocks and Mutual Fund Investments $226,589

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2002. Stocks owned by the company are located in the company’s safety deposit box.

Stock certificates were physically examined by the examiners. Stock and mutual fund purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in stocks and mutual funds was not in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Dividends received during 2002 on stocks and mutual funds amounted to $6,596 and were traced to cash receipts records. Accrued dividends of $442 as of December 31, 2002, were checked and allowed as a non-ledger asset.

The investment rule prescribes that a town mutual cannot hold more than an aggregate of 10% of admitted assets in Type 1 Preferred Stock, or in Money Market Mutual Funds, or 3% in any one investment.

1.	Admitted Assets x .10	$47,474
2.	Admitted Assets x .03	14,242

As of year-end 2002, the company had investments in Type 1 Preferred Stock with a statement value of $62,584. This exceeded the 10% limitation contained in the investment rule by $15,110. At the time of this examination, two of these investments were sold which brought the company into compliance with this rule.

As of year-end 2002, the company had investments in Type 1 Money Market Funds with a statement value of $68,186. This exceeded the 10% limitation by $20,712. The prior examination also found that the company had exceeded the 10% limitation on investments in money market funds. It is again recommended that the company divest itself of any investment that does not comply with s. Ins 6.20 (6) (b), Wis. Adm. Code.

Agents' Balances or Uncollected Premiums $3,943

The above ledger asset represents the amounts due from policyholders which are not in excess of 90 days past due at year-end. A review of individual accounts verified the accuracy of this asset.

Premium - Installments Booked But Deferred Not Yet Due $56,596

The above asset represents the amount of installments booked for the remainder of the policy period, but not due to the company at year-end. Review of the policyholders' balances verified the reasonableness of the asset.

Investment Income Due and Accrued $2,797

Interest due and accrued on the various assets of the company as of December 31, 2002, consists of the following:

Cash at Interest	$ 22
Bonds	2,333
Stock	442
	$2,797

A review of individual investment accounts verified the accuracy of this asset.

Reinsurance Recoverable on Paid Losses **$2,457**

The above asset represents recoveries due to the company from reinsurance on losses which were paid on or prior to December 31, 2002. A review of year-end accountings with the reinsurer verified the above asset.

Equipment Data Processing Equipment **$411**

This asset represents the admitted asset portion of EDP equipment, which excludes non-operating system software owned by the company as of December 31, 2002. Review of the equipment balances and depreciation schedules indicated the equipment is properly valued at year-end.

Reinsurance Contingent Commission Receivable **$2,962**

This asset represents contingent commissions due the company for premium ceded to its reinsurer. Review of the year-end accounting with the reinsurer verified the accuracy of this asset.

Equipment, Furniture, and Supplies **$0**

This asset consists of $1,573 of office equipment owned by the company as of December 31, 2002. In accordance with annual statement requirements, this amount has been deducted as a non-admitted asset.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$57,924**

This liability represents losses incurred on or prior to December 31, 2002, and remaining unpaid as of that date. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule.

	Company Estimate	Examiners' Development	Difference
Incurred But Unpaid Losses	$287,226	$187,319	$99,907
Less:			
Reinsurance Recoverable on Unpaid Losses	(224,361)	(129,395)	(94,966)
Net Unpaid Losses	$ 62,865	$ 57,924	$ 4,941

The examiner developed this liability by totaling actual loss payments made through the development period on those losses incurred on or prior to December 31, 2002. To the actual paid loss figures was added an estimated amount for those 2002 and prior losses remaining unpaid at the examination date. Surplus was adjusted for the above difference of $4,941 and is included in the Reconciliation of Policyholders' Surplus section of this report.

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and all claims which were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proper proof of loss. In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

After reviewing the company's claim files, it was noted that the internal adjusters were not completing the adjusting report form on every claim. It is recommended that the company have its adjusters complete this form to show what investigations were done, to document compliance with, and to avoid the unfair claims settlement practices described in s. Ins 6.11 (3) (b) 3., Wis. Adm. Code.

Unpaid Loss Adjustment Expenses **$663**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2002, but which remained unpaid as of year-end. The methodology used by the company in establishing this liability is an estimate based on an average of prior year's payments of unpaid loss adjustment expenses.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be reasonably stated.

Fire Dues Payable **$528**

This liability represents the fire department dues payable as of December 31, 2002. The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount paid was verified by a review of the cash disbursement records and the commissioner's records for fire dues paid.

Unearned Premiums **$161,124**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was established using a daily pro rata methodology. The examiner reviewed the company's calculation of this liability and determined it to be adequately stated.

Reinsurance Payable **$42,193**

This liability consists of amounts due to the company's reinsurer as of December 31, 2002, relating to transactions which occurred on or prior to that date.

The following is the reinsurance payable balance at year-end.

Class A Non-property	$ 8,499.
Class B First Surplus	19,744.
Class C Excess of Loss	10,550.
Class D/E Stop Loss	3,400.
	$42,193.

Subsequent cash disbursements and reinsurance accountings verified the amount of this liability.

Amounts Withheld for the Account of Others **$979**

This liability represents employee payroll deductions in the possession of the company as of December 31, 2002. Supporting records and subsequent cash disbursements verified this item.

Payroll Taxes Payable **$298**

This liability represents the company's portion of payroll taxes incurred prior to December 31, 2002, which had not yet been paid. Supporting records and subsequent cash disbursements verified this item.

Accounts Payable **$127**

This liability consists of amounts due to creditors for office and miscellaneous expenses as of December 31, 2002. Supporting records and subsequent cash disbursements verified this item.

Accrued Property Taxes **$66**

This liability consists of amounts due for property taxes to the village where the company's office is located. Supporting records and subsequent cash disbursements verified this item.

Pension Payable **$75**

This liability represents the amounts due for the employee's savings incentive match plan (SIMPLE) as of December 31, 2002, which had not yet been paid. Supporting records and subsequent cash disbursements verified this item.

Premiums Received in Advance **$4,602**

This liability consists of amounts received for premiums in advance of their effective date. Supporting records and cash receipts verified this item. The company also included premium received in advance for policy installment payments. These premium receipts are already accounted for in the unearned premium calculation, and are double counted by including them here. It is recommended that the company not include payments received for the policies on the multiple payment plans in the Advance Premium balance reported on the Annual Statement.

The Premium Received in Advance liability was reduced by $1,099 with a corresponding entry made to surplus in the Reconciliation of Policyholder’s Surplus section of this report.

V. CONCLUSION

As of December 31, 2002, the company reported assets of $474,739, liabilities of $275,718, and Policyholders’ Surplus of $199,021. The reported Policyholders’ Surplus of $199,021 is below the $200,000 surplus requirements of section Ins 13.06 (4), Wis. Adm. Code. Further action may be necessary by the office should the company continue to violate this section of the rule. There were two examination reclassifications reducing liabilities and increasing surplus of $6,040 as the result of this examination.

In the four years since the prior examination, gross premiums written have increased by 35%. During the same period, net premiums written have increased by 32%, but surplus has decreased by 45%. The company reported underwriting losses in all of the last six years due to multiple fire losses in all years except 2001. Due to these underwriting losses, the company was able to post only one positive net income in the last six years. To increase income and reduce costs for 2003, the company is reviewing its policy rates, increased its policy fee, increased its wood surcharge, increased its home owners minimum insured amount, and increased policy deductibles to $250 while eliminating the 10% discount associated with selecting this deductible and kept salaries and reimbursements at prior year levels.

The current examination resulted in one suggestion, one repeat and four new recommendations. The suggestion and recommendations are summarized in the following section of this report.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 18 — Policy Cancellations — It is suggested that the company alter its 2nd and final notice of cancellation in order to limit the company's risk of claims after the policy has been canceled due to non-payment.

2. Page 18 — Accounts and Records — It is recommended that the company adhere to its policy regarding check signatures in compliance with s. 13.05 (4) (b), Wis. Adm. Code.

3. Page 20 — Investment Rule Compliance — It is recommended that the company's board of directors adjust its written investment plan to comply with the investment rule in accordance with s. Ins 6.20 (6) (c), Wis. Adm. Code, and that the company refrain from any purchases of investments not in compliance until an excess of Type 1 investments is attained.

4. Page 23 — Stocks and Mutual Fund Investments — It is again recommended that the company divest itself of any investment that does not comply with s. Ins 6.20 (6) (b), Wis. Adm. Code.

5. Page 25 — Net Unpaid Losses — It is recommended that the company have its adjusters complete this form to show what investigations were done, to document compliance with, and to avoid the unfair claims settlement practices described in s. Ins 6.11 (3) (b) 3., Wis. Adm. Code.

6. Page 27 — Premiums Received in Advance — It is recommended that the company not include payments received for the policies on the multiple payment plans in the Advance Premium balance reported on the Annual Statement.

VII. ACKNOWLEDGMENT

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

Respectfully submitted,

Russell Lamb
Examiner-in-Charge